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**Queensland  
Government**

Your Ref: MBN1280  
Our Ref:

Department of  
**Mines and Energy**

Mr Brian Parmenter  
Chairman  
Queensland Competition Authority  
GPO Box 2257  
BRISBANE QLD 4001

Dear Mr Parmenter

The Department of Mines and Energy (DME) welcomes the opportunity to provide comment on the Queensland Competition Authority's (QCA) *Draft Decision on the Benchmark Retail Cost Index (BRCI) for Electricity: 2009-10* (the Draft Decision).

The Queensland Government maintains an objective of fostering competition in the energy market so that the economy and customers derive the benefits of a competitive energy sector. Efficient and sustainable energy pricing is essential to meeting these objectives, particularly in the face of sustained and significant growth in electricity demand across the State.

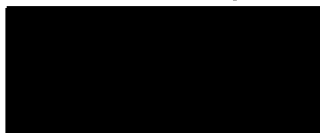
DME has reviewed the Authority's Draft Decision and has provided a submission for your consideration.

Consistent with previous submissions, the Government wishes to emphasise that only genuine cost increases should be passed onto consumers through the application of the BRCI.

DME fully supports the QCA's decision not to include costs associated with emissions trading within the 2009-10 electricity pricing regime. The Commonwealth Government's White Paper which was released on 15 December 2008, has provided clear guidance on the start date for the Carbon Pollution Reduction Scheme and as such, it should not be included in the 2009-10 pricing considerations.

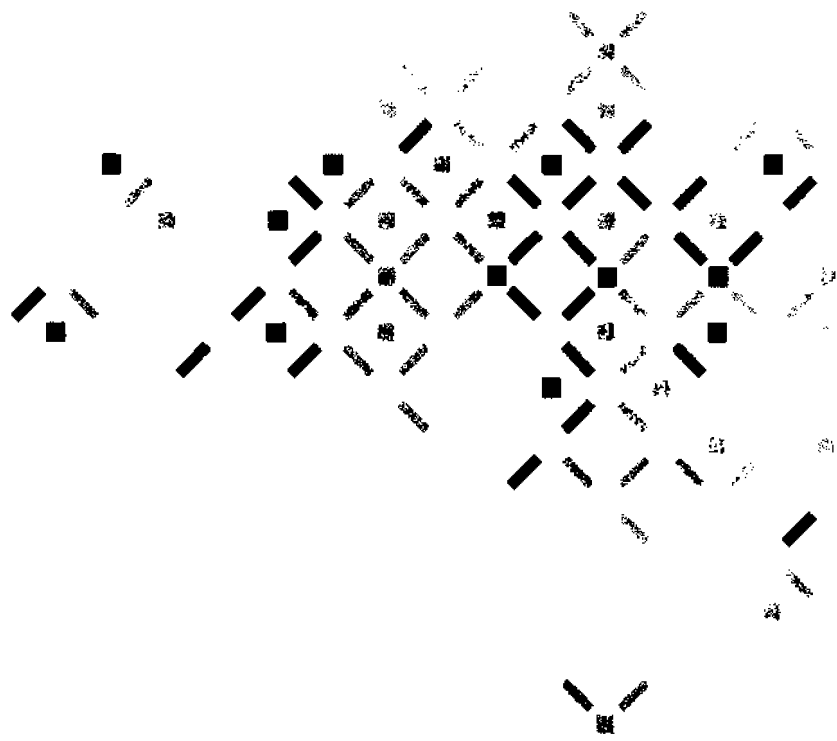
I thank you for your consideration of these matters. Should you have any enquiries they should be directed to Ms Michelle Norris, Director, Policy Division, telephone 3225 8256.

Yours sincerely



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**Director General**  
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# **Submission to the Queensland Competition Authority**

Response to the Draft Decision on  
the Benchmark Retail Cost Index  
(BRCI) for Electricity 2009-10

Prepared by the Department of Mines and  
Energy

19 December 2008

## **Introduction**

The Department of Mines and Energy (DME) welcomes the opportunity to provide comment on the Queensland Competition Authority's (QCA) *Draft Decision on the Benchmark Retail Cost Index (BRCI) for Electricity: 2009-10* (the Draft Decision).

The Queensland Government maintains its objective of fostering competition in the energy market so that the economy and customers derive the benefits of a competitive energy sector. Efficient and sustainable energy pricing is essential to meeting these objectives, particularly in the face of significant growth in south-east Queensland.

However, DME is also mindful that only genuine cost increases should be passed on to consumers through the application of the BRCI. The price of electricity in Queensland has always been competitive when compared to other States and it is important to maintain that position.

The *Electricity Act 1994* provides that the "...total benchmark retail cost, expressed in cents per kilowatt hour for the relevant tariff year is the estimated total cost of supplying customers in the State for that year..." (S. 91G(1)). The Queensland Government recognises that price increases should be kept to the minimum necessary to reflect increases in the cost of supply. Queensland's electricity consumers should be protected from price rises which are not absolutely necessary. On the other hand, the Queensland Government acknowledges that unless prices rise in line with costs, the future reliable supply of electricity to consumers would be threatened.

DME recognises the importance of setting notified electricity prices to reflect only changes in the true costs of electricity supply. The Government for its part will look to assist electricity consumers to conserve energy and reduce their carbon footprint through increased energy efficiency and awareness of energy usage patterns.

## **Background**

In line with previous submissions to the QCA, DME reiterates that notified electricity prices will remain an important feature of Queensland's electricity market. This 'safety net' policy is especially important for customers in regional locations where the cost of supply is higher than the notified prices actually charged to customers, and as a result is subsidised by the Queensland Government.

A consumer protection feature of the legislation is that a small customer's existing retailer must supply electricity at the notified price if the customer chooses to revert to a standard contract at the conclusion of a market contract. This should not result in the customer's retailer then having to supply electricity at a loss.

## **Energy Costs**

Energy costs account for around half of the increase in the 2009-10 BRCI (6.80 percentage points) in the Draft Decision.

Section 92(1-2) of the Act provides that the cost of energy must reflect the pricing entity's view of the likely total of the costs to be incurred during the relevant tariff year to supply all of the National Electricity Market (NEM) load of the State. This view must be based on "the pricing entity's most recent estimate of the Long Run Marginal Costs (LRMC) of energy in the part of the State connected to the national grid" and must "take into account the most efficient combination of generation plant to supply all of the NEM load for the State for the relevant tariff year".

This legislative requirement is based on the theory that, over a sufficiently long period of time, average energy purchase costs should broadly equal the LRMC of generation, as periods of surplus and deficit capacity are balanced. However, in any given year, the purchase cost of energy may be higher or lower than the LRMC and the QCA has the discretion to also take into account the actual cost of purchasing energy in the State for a particular year. In this regard, the short-run, actual energy purchase costs incurred by a retailer will almost certainly differ from the LRMC of energy because of factors such as supply-demand imbalances and pre-existing hedge portfolios. In considering these issues, the QCA decided to apply a 50% weighting to each of the LRMC and short-run energy purchase cost within the cost of energy component, consistent with the approach in 2008-09. DME considers this approach to balancing the short run and long run marginal costs of energy production to be consistent with the legislation.

In calculating the LRMC for 2009-10, the QCA has again had regard to the costs of supply to the whole of the Queensland load and Queensland's integral position within the National Electricity Market. DME is strongly supportive of this approach which reflects the reality of the situation as well as the "most efficient combination of generation plant to supply all of the NEM load for the relevant tariff year".

DME considers that the inclusion of the costs associated with the 13% Gas Scheme, the Commonwealth's Renewable Energy Target including its expansion to the extent it applies in 2009-10, NEM participant fees and ancillary services charges from the National Electricity Market Management Company (NEMMCO), are consistent with the legislation.

### **Emissions Trading**

The Commonwealth Government has released a White Paper describing its policy position on the Carbon Pollution Reduction Scheme (CPRS). In particular, it has announced that the commencement date will be 1 July 2010. DME supports the QCA's position not to include any costs associated with the CPRS in the 2009-10 pricing regime. However, DME considers it is not possible to rule out that some increased costs are already being priced into the market through generators' risk profiles and impacts on availability of long term contracts.

### **Network Charges**

In the Draft Decision, network costs account for around 42% of the total increase in the 2009-10 BRCI (5.82 percentage points).

The Act states that the network cost component of the BRCI "must reflect the pricing entity's view of the likely total revenue requirements for the relevant tariff year for transmission entities and distribution entities in the State" (s93(1)).

The network cost component of the BRCI is calculated based on the Australian Energy Regulator's (AER) determination of Powerlink's 2007-08 to 2011-12 transmission revenue requirements, and QCA's determination of 2005-06 to 2009-10 distribution network revenues for ENERGEX and Ergon Energy. Approved cost pass-throughs are included. Recent published decisions by the QCA approved pass-through of Cyclone Larry costs for Ergon Energy and Full Retail Contestability costs for ENERGEX, which have been included in the cost base.

The annual change in network costs is calculated by adding together the Aggregate Annual Revenue Requirement (AARR) of ENERGEX and Ergon Energy, including Powerlink's charges, and calculating an average increase in network costs for the State. In aggregate, network costs increase by 10.5% between 2008-09 and 2009-10.

Despite suggestions from other parties that the averaging approach results in a deterioration of headroom, which reduces the ability of retailers to compete for those customers, DME believes the QCA's approach to the calculation of network costs is consistent with the approach prescribed by the legislation and the Minister's amended Delegation of 11 March 2008.

### **Retail Costs**

In the Draft Decision, retail costs account for around seven per cent of the increase in the 2009-10 BRCI (1.01 percentage points).

According to s94 of the Act, retail costs "must reflect the pricing entity's view of the likely cost of providing customer retail services to Queensland customers connected to the national grid, based on an efficient entity carrying on an electricity retail business that meets all of the following criteria: it is carried on separately from other business; it has a significant share of the State's electricity retail market; it provides customer retail services to a cross-section of customers; it earns a reasonable retail margin."

Retail costs are associated with billing, customer call centres, credit management, energy trading activities, corporate overheads, information technology systems, customer acquisition costs and compliance costs.

The QCA has adopted a retail margin of five per cent in calculating the retail cost component in all three tariff years (2007-08, 2008-09 and 2009-10). The QCA notes in its Draft Decision that retail margins in other jurisdictions ranged from two to eight per cent.

DME notes that a number of retailers provided submissions earlier in the consultation process for 2009-10 which indicated that the five per cent allowance was an insufficient margin. The QCA has maintained a view that there was no strong evidence that a reasonable margin sought by retailers for 2009-10 would be materially different from that applicable to the Queensland market in 2008-09.

DME considers the QCA's approach to calculating retail costs is consistent with the relevant legislation.

### **Conclusion**

In summary, DME emphasises the importance of ensuring that only true changes in the costs of electricity supply are passed onto consumers. It is acknowledged that if prices do not rise in line with the cost of supplying electricity, the secure provision of electricity to Queensland consumers - including households - is at risk. DME also acknowledges the QCA has a responsibility to ensure price rises are no greater than necessary to cover cost increases.

DME believes that the approaches taken by the QCA in determining the costs of energy, networks and retailing for the Draft Decision are consistent with the *Electricity Act 1994*.